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Washington, D.C. 20463

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FIRST GENERAL COUNSEL'S REPORT

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AUDIT REFERRAL: 11-03
DATE REFERRED: June 9, 2011
DATE ACTIVATED: September 19, 2011

EXPIRATION OF SOL:
Earliest September 24, 2013
Latest November 4, 2013

SOURCE: Internally Generated

RESPONDENTS: Freedom's Defense Fund and Scott B. MacKenzie,
in his official capacity as treasurer

RELEVANT STATUTES
AND REGULATIONS: 2 U.S.C. § 431(17)
2 U.S.C. § 434(b)(6)(B)(iii) and (g)
11 C.F.R. § 100.22(a)
11 C.F.R. § 104.3(b)(3)(vii)
11 C.F.R. § 104.4(a),(b) and (c)
11 C.F.R. § 104.14(b)(1)

INTERNAL REPORTS CHECKED: Audit Documents
Disclosure Reports

FEDERAL AGENCIES CHECKED: None

I. INTRODUCTION

The Audit Division referred this matter to the Office of General Counsel following an audit of the Freedom's Defense Fund's ("FDF") activity from January 1, 2007 through December 31, 2008. See 2 U.S.C. § 438(b). The Final Audit Report ("FAR"), approved by the Commission on May 27, 2011, contained one finding related to FDF's failure to correctly disclose all of its independent expenditures on Schedule E of its reports filed with the Commission and its failure to file appropriate 24- and 48-Hour Notices of Independent

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Expenditures.¹ On June 22, 2011, this Office notified the Respondents of the referral in accordance with the Commission's policy regarding notification in non-complaint generated matters. 74 Fed. Reg. 38617 (August 4, 2009). FDF did not submit a response to the Commission's notification.

We recommend that the Commission open a Matter Under Review, find reason to believe that FDF and Scott B. MacKenzie, in his official capacity as treasurer, violated 2 U.S.C. § 434(b)(6)(B)(iii) and (g) and 11 C.F.R. § 104.4(b) and (c), and enter into pre-probable cause conciliation with FDF.

II. FACTUAL AND LEGAL ANALYSIS

A. Facts

FDF is a multi-candidate committee that has been filing reports with the Commission since July 2004. Pursuant to 2 U.S.C. § 438(b), the Commission authorized an audit of FDF's activity from January 1, 2007 through December 31, 2008. In the normal course of the audit, the Audit Division reviewed FDF's disbursements for media buys during that time period. This review indicated that FDF disbursed \$62,499 in connection with a television advertisement entitled "What Murtha Says, Out of Touch" ("Murtha ad" or the "ad"), which was broadcast in Pennsylvania from September 22, 2008 through November 3, 2008.²

The advertisement regards the 2008 Congressional election in the 12th Congressional District of Pennsylvania and the 2008 Presidential election. The ad contains audio clips of then

¹ The FAR is available on the Commission's website. See *Audit Report – Freedom's Defense Fund*, http://www.fec.gov/audits/2008/AuditReport_2008_FreedomDefenseFund.shtml.

² The ad can be viewed on FDF's YouTube Channel, <http://www.youtube.com/user/FreedomDefenseFund#p/u/12/F2sccXXq8OU>.

1 Presidential candidate Senator Barack Obama and Congressional candidate Rep. John Murtha
2 making negative statements about people from Western Pennsylvania and urges viewers, "On
3 election day, tell Jack Murtha and Barack Obama what we think of them." The ad ends with a
4 verbal and a printed statement to "Vote Republican," and displays a photograph of candidates
5 John McCain and Sarah Palin.

6 On October 30, 2008, FDF filed a 24-Hour Notice disclosing \$19,001 in independent
7 expenditure-related disbursements to NCC Washington and Red Cap Strategies for the Murtha
8 ad. On December 4, 2008, FDF filed its 2008 Post-General Election Report, which included a
9 Schedule E (Itemized Independent Expenditure Form) disclosing the \$19,001 in disbursements
10 that FDF previously disclosed on the 24-Hour Notice. FDF did not disclose that it made any
11 additional expenditures in connection with the Murtha ad in that report or in any of the
12 subsequent reports it filed with the Commission covering the relevant time period.

13 The Interim Audit Report ("IAR") concluded that FDF disbursed \$60,397 in connection
14 with the Murtha ad,³ that the ad clearly identified candidates Murtha and Obama, and that the ad
15 expressly advocated their defeat in the general election. IAR at 5. The ad also clearly identified
16 then-candidates Senator John McCain and Sarah Palin, and advocated their election. The Audit
17 Division concluded that the Murtha ad constituted an independent expenditure, but that FDF
18 failed to properly disclose all of the costs associated with the ad and also failed to file
19 appropriate 24- and 48-hour notices of independent expenditures. At the time of the IAR, the
20 Audit Division determined that FDF had disclosed only \$19,001 of the \$60,397 expenditure and
21 disclosed the remaining disbursements made in connection with the Murtha ad as operating

³ As explained *infra*, the audit later determined that the actual cost of the Murtha ad was \$62,499.

1 expenditures. The IAR recommended that FDF amend its FEC reports to disclose the additional
2 \$41,396 of independent expenditures made in connection with the Murtha ad.

3 In response to the IAR, FDF amended its reports to disclose additional independent
4 expenditures related to the Murtha ad on Schedule E forms included with its 2008 Amended Pre-
5 General, Post-General, and Year-End Reports. FDF indicated that an additional \$2,102 of
6 expenditures that previously lacked documentation were actually associated with the Murtha ad,
7 bringing the total expenditures relating to the Murtha ad to \$62,499 (\$43,498 of which had not
8 been properly disclosed). Of the amount spent on the Murtha ad that the Audit Division
9 identified as requiring disclosure, however, FDF reported only an additional \$31,629 in vendor
10 payments, failing to disclose \$11,869 of the disbursements. See Attachment 1 at 4. Further,
11 FDF did not file the appropriate 24- or 48-hour notices for any of the disbursements that it
12 originally reported as operating expenses. *Id.* In addition, because FDF was unable to provide
13 precise dissemination dates for the independent expenditures and failed to maintain sufficiently
14 detailed documentation in order to associate the Murtha ad with the specific invoices, the Audit
15 Division could not determine the number of 24-hour or 48-hour notices that FDF should have
16 filed. See Attachment 1 at 3-4.

17 On May 27, 2011, the Commission approved the FAR's finding that FDF did not disclose
18 all independent expenditures and did not file all required notices for independent expenditures
19 made. Specifically, FDF failed to report \$11,869 in independent expenditures and failed to file
20 appropriate 24/48-hour notices for independent expenditures totaling as much as \$43,498.

21 **B. Analysis**

22 An independent expenditure is an expenditure that expressly advocates the election or
23 defeat of a clearly identified Federal candidate and that is not made in concert or cooperation

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1 with, or at the request or suggestion of, the candidate or his or her committee or agent. 2 U.S.C.
2 § 431(17). A political committee must disclose on a Schedule E the name of a person who
3 receives any disbursement during the reporting period in an aggregate amount or value in excess
4 of \$200 within the calendar year in connection with an independent expenditure by the reporting
5 committee, together with the date, amount, and purpose of any such independent expenditure and
6 a statement that indicates whether such independent expenditure is in support of or in opposition
7 to a candidate, as well as the name and office sought by such candidate. 2 U.S.C.
8 § 434(b)(6)(B)(iii); 11 C.F.R. §§ 104.3(b)(3)(vii) and 104.4(a). Committees are also required to
9 maintain records that provide information with sufficient detail so that the reports may be
10 verified. 11 C.F.R. § 104.14(b)(1).

11 A political committee that makes or contracts to make independent expenditures
12 aggregating \$10,000 or more in connection with a given election at any time during a calendar
13 year up to and including the 20th day before the date of an election shall file a report describing
14 the expenditures within 48 hours. 2 U.S.C. § 434(g)(2); 11 C.F.R. § 104.4(b)(2). These reports,
15 known as 48-Hour Notices, must be filed by the end of the second day "following the date on
16 which a communication that constitutes an independent expenditure is publicly distributed or
17 otherwise publicly disseminated." 11 C.F.R. § 104.4(b)(2). A committee is required to file
18 additional reports within 48 hours after each time it makes or contracts to make independent
19 expenditures aggregating an additional \$10,000. *Id.*

20 A political committee that makes or contracts to make independent expenditures
21 aggregating \$1,000 or more in connection with a given election after the 20th day, but more than
22 24 hours before the date of an election, is required to file a report describing the expenditures
23 within 24 hours. 2 U.S.C. § 434(g)(1); 11 C.F.R. § 104.4(c). These reports, known as 24-Hour

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1 Notices, must be filed within 24 hours "following the date on which a communication that
2 constitutes an independent expenditure is publicly distributed or otherwise publicly
3 disseminated." 11 C.F.R. § 104.4(c). The committee must file additional reports within 24
4 hours after each time it makes or contracts to make independent expenditures aggregating an
5 additional \$1,000. *Id.*

6 An ad contains express advocacy if it uses phrases such as "vote for the President" or
7 "defeat" accompanied by a picture of one or more candidates, or if it contains campaign slogans
8 or individual words, "which in context can have no other reasonable meaning than to urge the
9 election or defeat of one or more clearly identified candidate(s)." 11 C.F.R. § 100.22(a).

10 Here, the Murtha ad clearly identifies McCain and Palin by name and is accompanied by
11 a photograph and by the exhortation to "Vote Republican Tuesday November 4th." *Supra* at 3.
12 As concluded in the FAR, the ad "provides in effect a specific directive: vote for these pictured
13 candidates. The fact that this message is marginally less direct than 'Vote for Smith' does not
14 change its essential nature." *See* FAR at fn. 4 (quoting *FEC v. Massachusetts Citizens for Life*
15 *Inc.*, 479 U.S. 238, 239 (1986)). The ad expressly advocates the election of McCain and Palin.
16 *See also* OGC and Office of Compliance Memorandum to Commission dated July 26, 2010,
17 pertaining to Draft Interim Audit Report on Freedom's Defense Fund (LRA 810) ("IAR
18 Memorandum"), at 3 (analyzing whether the Murtha ad contained express advocacy).⁴

19 Because the Murtha ad contains express advocacy, FDF was required to report
20 disbursements associated with it as independent expenditures. The Audit Division's review of

⁴ The ad also urges the defeat of Murtha and Obama by identifying them by name and photograph and with audio clips of the candidates that portray them in a negative light, asking voters to "tell Jack Murtha and Barack Obama what [they] think of them" on election day, and urging voters to "Vote Republican." Asking voters to take these actions can have no reasonable meaning other than to vote against Obama and Murtha. *See* IAR Memorandum, at 3. Thus, the ad also expressly advocates the defeat of Obama and Murtha.

1 documentation provided by FDF established that FDF did not fully disclose the costs associated
2 with the Murtha ad as independent expenditures on Schedule E forms filed with the Commission.
3 Although FDF amended its reports in response to the IAR, \$11,869 of the total \$62,499 in
4 disbursements associated with the Murtha ad have not yet been properly disclosed on a Schedule
5 E. *Supra* at 3. Further, the audit established that 24- and 48-hour notices of independent
6 expenditures were required for the \$62,499 in costs for the Murtha ad, but that FDF disclosed
7 only \$19,001 in such notices. Therefore, FDF failed to file required notices for expenditures
8 totaling \$43,498.

9 Based on the foregoing, we recommend that the Commission find reason to believe that
10 FDF and Scott B. MacKenzie, in his official capacity as treasurer, violated 2 U.S.C.
11 § 434(b)(6)(B)(iii) and (g) and 11 C.F.R. § 104.4(b) and (c), by failing to disclose independent
12 expenditures in reports filed with the Commission and failing to file appropriate 24-Hour or
13 48-Hour Notices of Independent Expenditures.

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IV. RECOMMENDATIONS

1. Open a MUR;
2. Find reason to believe that Freedom's Defense Fund and Scott B. MacKenzie, in his official capacity as treasurer, violated 2 U.S.C. § 434(b)(6)(B)(iii) and (g), and 11 C.F.R. § 104.4(b) and (c);
3. Approve the attached Factual and Legal Analysis;
4. Enter into conciliation with Freedom's Defense Fund and Scott B. MacKenzie, in his official capacity as treasurer, prior to a finding of probable cause to believe;
- 5.
6. Approve the appropriate letter.

Anthony Herman
General Counsel

2-16-12
Date

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Peter G. Blumberg
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Attachments:

1. Audit Referral



FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

June 9, 2011

MEMORANDUM

To: Christopher Hughey
Acting General Counsel

Through: Alec Palmer
Acting Staff Director

From: Patricia Carmona *PC*
Chief Compliance Officer

AUDIT REFERRAL # 11-63

Joseph F. Stoltz
Assistant Staff Director
Audit Division

Thomas Himmelfarb
Deputy Assistant Staff
Director for Public Financing

Alex R. Boniewicz
Audit Manager

Alex R
Boniewicz

By: Tesfai Asmamaw
Lead Auditor

Tesfai Asmamaw

Subject: Freedom's Defense Fund (A09-21) - Referral Matter

On May 25, 2011, the Commission approved the final audit report on Freedom's Defense Fund. The final audit report includes the following matter that is referable:

Finding 1 – Disclosure of Independent Expenditures

All work papers and related documentation are available for review in the Audit Division. Should you have any questions regarding this matter, please contact Jim Miller or Alex Boniewicz at 694-1200.

Attachment: Finding 1 – Disclosure of Independent Expenditures

cc: Lorenzo Holloway

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Disclosure of Independent Expenditures

Summary

During audit fieldwork, the Audit staff reviewed FDF's disbursements for media buys and questioned \$97,896 of the disbursements. Of this amount, FDF had reported \$19,001 as independent expenditures and \$78,895 as operating expenditures. In response to the Interim Audit Report, FDF provided documentation demonstrating that the costs of the independent expenditures were \$62,499. FDF also amended its reports to correctly disclose all but \$11,869 of this amount as independent expenditures. Appropriate 24/48-hour notices were not filed for independent expenditures totaling as much as \$43,428. The Commission approved this finding.

Legal Standard

A. Independent Expenditures. An independent expenditure is an expenditure made for a communication expressly advocating the election or defeat of a clearly identified candidate that is not made in cooperation, consultation, or concert with, or at the request or suggestion of, a candidate, a candidate's authorized committee, or their agents, or a political party or its agents.

A clearly identified candidate is one whose name, nickname, photograph or drawing appears, or whose identity is apparent through unambiguous reference, such as "your Congressman," or through an unambiguous reference to his or her status as a candidate, such as "the Democratic presidential nominee" or "Republican candidate for Senate in this state."

Expressly advocating means any communication that:

- Uses phrases such as "vote for the President" or "re-elect your Congressman" or communications of campaign slogan(s) or individual word(s), which in context can have no other reasonable meaning than to urge election or defeat of one or more clearly identified candidates; or
- When taken as a whole and with limited reference to external events, such as proximity to the election, could be interpreted by a reasonable person only as advocating the election or defeat of one or more clearly identified candidates. 11 CFR §§100.16(a), 100.17 and 100.22.

B. Reporting Independent Expenditures. When independent expenditures to the same person exceed \$200 in a calendar year, the committee must report on Schedule E (Itemized Independent Expenditures):

- Amount;
- Date when the expenditures were made;
- Name and address of the payee;
- Purpose (a brief description of why the disbursement was made);
- A statement indicating whether the independent expenditure was in support of, or in opposition to, a particular candidate, as well as the name of the candidate and

the office sought (including State and Congressional district, when applicable); and,

- A certification, under penalty of perjury, as to whether the independent expenditure was made in cooperation, consultation or concert with, or at the request or suggestion of, any candidate or authorized committee or agent of such committee. 2 U.S.C. §434(b)(5)(B)(iii) and 11 CFR §104.3(b)(3)(vii).

C. 24/48-Hour Reporting Notices for Independent Expenditures. Political committees and others making independent expenditures at any time during the calendar year—up to and including the 20th day before an election—must disclose this activity within 48 hours of the date on which the public communication is disseminated each time that the expenditures aggregate \$10,000 or more. In addition, independent expenditures that aggregate \$1,000 or more during the last 20 days—up to 24 hours—before an election require disclosure within 24 hours following the dissemination date. 2 U.S.C. §434(d) and (g); 11 CFR §104.4(b).

D. Requirements for Maintaining Records. Reporting committees are required to maintain records that provide, in sufficient detail, the information from which the filed reports may be verified. 11 CFR §104.14(b)(1).

Facts and Analysis

A. Facts

During audit fieldwork, the Audit staff reviewed disbursements made by FDF for media¹. FDF disbursed \$97,896 for certain media buys, reporting \$19,001 as Independent Expenditures on Schedule E and in 24/48-hour notices, and \$78,895 as operating expenditures.

1. Documented Media Buys

An ad, titled "What Murtha Says, Out of Touch" (Murtha ad), was aired in Pennsylvania from 09/22/2008 to 11/03/2008, at a cost of \$60,397. Of this amount, FDF reported \$19,001 as independent expenditures and the remaining \$41,396 as operating expenditures. The ad clearly identified Rep. John Murtha and then-Presidential candidate Barack Obama, and expressly advocated their defeat. The ad also clearly identified then-Presidential candidate John McCain and Vice Presidential candidate Sarah Palin, and advocated their election. The Audit staff concluded that the Murtha ad was an independent expenditure and FDF should have reported it as such and filed the appropriate 24/48-hour notices.

¹ Pursuant to Commission Directive 69, Legal Guidance to the Office of Compliance, the Office of Compliance and the Office of General Counsel submitted a memorandum to the Commission asking guidance as to whether certain advertisements broadcast by FDF contained express advocacy and the costs were therefore independent expenditures. The Commission was unable to consider the issue within 60 days of that memorandum; therefore, pursuant to Directive 69, the audit report was prepared consistent with the staff analysis. *Commission Directive 69 is Available at http://www.fec.gov/directives/directive_69.pdf*

The Murtha ad begins with a narrator's declaration that "Barack Obama and Jack Murtha have little respect for the people of Western Pennsylvania." It then contains audio clips of Obama and Murtha making negative statements about Western Pennsylvanians. Murtha is heard saying: "There's no question that Western Pennsylvania is a racist area," and Obama is heard saying that Pennsylvanians "get bitter and cling to guns and religion." Next, the text on the screen reads "MURTHA AND OBAMA DON'T REPRESENT OUR VALUES," as the narrator says: "On election day, tell Jack Murtha and Barack Obama what we think of them." The narrator ends with the statement "Vote Republican" while a picture of McCain and Palin appears and the text on the screen reads "VOTE REPUBLICAN TUESDAY, NOVEMBER 4TH."² The ad concluded with an appropriate disclaimer for an independent expenditure.

Of the \$60,397 FDF reported spending on the Murtha ad, FDF provided dissemination information for costs totaling \$34,028. These ads ran from October 21 through November 3, 2008. Notices filed for reported independent expenditures of \$19,001 disclosed a communication date of October 29, 2008, indicating that these notices are related to ads for which dissemination dates were made available. However, the Audit staff was unable to associate the dissemination date and amounts on the 24/48-hour notices with dates and amounts on the supporting documentation. The Audit staff's review of the available information indicated that FDF should have disclosed \$41,386 (\$60,397 - \$19,001) as independent expenditures rather than operating expenditures, and that FDF failed to file 24-hour notices for Murtha ad costs totaling \$15,027 (\$34,028 - \$19,001).

Dissemination information was not provided for the remaining \$25,369 (\$60,397 - \$34,028), which limited the Audit staff evaluation of the 24/48-hour notice requirements. Appropriate 24/48-notices appear to be required and were not filed.

2. Undocumented Media Buys

The Audit staff noted that media expenditures reported as operating expenditures, totaling \$37,499 (\$97,896 - \$60,397), lacked documentation and could not be associated with a specific ad or dissemination date.

B. Interim Audit Report & Audit Division Recommendation

The Audit staff addressed these expenditures at the exit conference and provided the FDF representative with a schedule detailing these expenditures. The FDF representative stated he would review the expenditures and contact the media vendor to request detailed analysis of the media buys. Subsequent to the exit conference, FDF provided some additional documentation, which was considered in the above analysis.

In the Interim Audit Report, the Audit staff recommended that FDF take the following action:

² "[I]t provides in effect a specific directive: vote for these pictured candidates. The fact that this message is marginally less direct than 'Vote for Smith' does not change its essential nature." *FEC v. Massachusetts Citizens for Life Inc. ("MCFL")* 479 U.S. 238, 239 (1986); 11 C.F.R. § 100.22(a).

- Provide any other documentary evidence that would demonstrate that these disbursements were not independent expenditures; or
- Provide documentation that details dissemination dates for these media buys that lack such information and, for those expenditures (\$37,499) for which no documentation has been made available;
- Provide documentation that associates these costs with specific media ads and, if the costs are related to the Murtha ad or communications that contain express advocacy, details dissemination dates;
- Submit and implement revised procedures for reporting independent expenditures and for tracking dissemination dates for such expenditures to allow for timely filing of 24/48-hour reporting notices, as required; and
- Amend its reports to correct the reporting of independent expenditures, as noted above.

C. Committee Response to the Interim Audit Report

With respect to the \$37,499 in expenditures lacking documentation to determine the nature of the expense, FDF provided information associating some of these costs with the Murtha ad (\$2,102) and demonstrating that the others (\$35,397) were not independent expenditures.

FDF submitted written procedures for reporting independent expenditures and for tracking dissemination dates for such expenditures to allow for timely filing of 24/48-hour notices, and indicated its intent to implement these procedures immediately.

FDF also amended its reports to disclose additional independent expenditures totaling \$31,629.

FDF's independent expenditures related to the Murtha ad totaled \$62,499 (\$60,397 + \$2,102). FDF disclosed independent expenditures of \$50,630 for the Murtha ad (\$19,001 + \$31,629). FDF did not correctly disclose as independent expenditures the remaining \$11,869 (\$62,499 - \$50,630). Audit staff advised FDF's representative of the difference but received no further explanation.

In connection with the \$62,499 in independent expenditures for the Murtha ad, it appeared that FDF did not file appropriate 24/48-hour notices for independent expenditures totaling \$43,498 (\$62,499 - \$19,001). Of the \$62,499 in independent expenditures for the Murtha ad, FDF was unable to provide dissemination dates for disbursements totaling \$28,471.

D. Draft Final Audit Report

In the Draft Final Audit Report, the Audit Staff acknowledged that amendments were filed, though incomplete; and, that written procedures to be implemented for reporting independent expenditures and tracking dissemination dates were submitted by FDF.

Commission Conclusion

On May 5, 2011, the Commission considered the Audit Division Recommendation Memorandum, in which, the Audit Division recommended that the Commission adopt a finding that FDF did not disclose all independent expenditures, and did not file all required notices for independent expenditures made.

The Commission approved the Audit Staff recommendation.

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